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# The Contract Clause of the United States Constitution

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## THE CONTRACT CLAUSE OF THE UNITED STATES CONSTITUTION

"No State shall pass any law impairing the obligation of contracts"—Article I, Section 10, Constitution of the United States.

### ORIGIN

It is reasonably safe to assert that there is perhaps no clause in the entire Constitution the origin and intendment of which is subject to greater obscurity and doubt. It has been variously interpreted by the courts and has always given rise to the greatest diversity of opinion among legal thinkers.

The Ordinance of 1787 passed by the Continental Congress for the government of the Northwestern Territory makes this provision:

"And in the just preservation of rights and property, it is understood and declared, that no law ought ever to be made or have force in said territory, that shall in any manner whatever interfere with or affect private contracts or engagements, bona fide and without fraud previously formed."

Since this was passed by the Continental Congress while the Constitutional Convention was in progress its chief significance lies in the fact that the necessity for the protection of private contracts seems to have had the sanction of contemporaneous thought.

It is worthy of note, however, that a proposal by Rufus King that the Convention should insert in the Constitution the above provision taken from the Ordinance of 1787 was defeated August 28, 1787 and the Rutledge substitute embracing a prohibition upon the power of the States to pass "any Bill of Attainder or ex post facto law" was adopted.<sup>1</sup> The Draft of the Committee of Five about three weeks earlier contained no reference to the Contract Clause. Neither did the plans of Pinckney, Hamilton or Paterson provide for any such restriction on the states.

The reason for the absence of any such provision is taken from Justice Miller:

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<sup>1</sup> V. Elliot's Debates 485.

"For the purpose of preventing any interference with contracts the Convention had relied very largely upon the clause prohibiting the passage of any *ex post facto* law."<sup>2</sup>

Dickinson, however, after consulting Blackstone, called the attention of the Convention to the fact that the term "*ex post facto*" related to criminal cases only. The report was passed over to the Committee on Style before any action was taken in regard to the matter. Rufus King, who had previously moved the adoption of the provision from the Ordinance of 1787 as a restriction upon the states, was a member of this committee. Gouverneur Morris, likewise a member of the Committee, is said to have added the words:

"No State shall pass laws 'altering' or impairing the obligation of contracts."

This report of the revision was submitted to the Convention on September 12, 1787. The Convention, itself, without debate, two days later amended the clause and put it in the form in which it now appears in the Constitution.<sup>3</sup>

As matters stood both Congress and the states were prohibited from passing Bills of Attainder and *ex post facto* laws, while the states were placed under the further restriction of the contract clause itself. It is interesting to note the following entry in the notes of Mr. Madison:

"Mr. Gerry entered into observations inculcating the importance of public faith, and the propriety of the restraint put on the States from impairing the obligation of contracts, alleging that Congress ought to be laid under the like prohibitions, he made a motion to that effect. He was not seconded."<sup>4</sup>

The foregoing facts give rise to some rather interesting conjectures and lead to the following inquiries:

1. If contracts were regarded by the Convention as protected by the *ex post facto* clause, then was it the intention to restrict Congress as well as the States? Evidently that was the intention since both were denied the power to pass *ex post facto* laws in identical language. If this be true then where is to be found the explanation for the change of view that occasioned the loss of Mr. Gerry's motion for want of a second?

2. If contracts were not regarded as protected by the *ex post facto* clause, then was there no prior intention to restrict either Congress or the States? Apparently there was no such intention. This

<sup>2</sup> Miller, Const. of U. S. 526.

<sup>3</sup> Bancroft, Hist. of Const., Vol. II, book 3, chapter 11.

<sup>4</sup> Madison Debates (Hunt and Scott) 567.

might explain the refusal of the Convention to adopt the King proposal of August 28, but would entirely fail to account for the action in adopting the report of the Committee, embracing the Contract Clause as a restriction upon the States, without debate.

Confusion results in the attempt to account for the action of the Convention under either hypothesis and leaves the contract clause to be interpreted as a mere matter of language without reference to what was intended to be accomplished by its adoption.

References to other sources for explanation are just as unsatisfactory. The clause is only twice mentioned in the *Federalist*. Mr. Hamilton makes this observation:

"Laws in violation of private contract, as they amount to aggressions on the rights of those States whose citizens are injured by them, may be considered as another probable source of hostility. . . . We have observed the disposition to retaliation excited in Connecticut, in consequence of the enormities perpetrated by the Legislature of Rhode Island."<sup>5</sup>

We are led to infer from this that the purpose back of the clause was to lessen the probability of hostility as between the states growing out of contracts between their citizens. There is not one word in regard to the inherent viciousness of state interference in private contracts that became the keynote of the early decisions in applying the provision.

Mr. Madison, on the other hand, seems to have fixed his gaze on future developments with prophetic vision. He wrote:

"Bills of Attainder, ex post facto laws, and laws impairing the obligation of contracts, are contrary to the first principles of the social compact, and to every principle of sound legislation. The two former are expressly prohibited by the declarations prefixed to some of the State Constitutions, and all of them are prohibited by the spirit and scope of these fundamental charters. Our own experience has taught us, nevertheless, that additional fences against these dangers ought not to be omitted. Very properly, therefore, have the Convention added this constitutional bulwark in favor of personal security and private rights; and I am much deceived if they have not, in so doing, as faithfully consulted the genuine sentiments as the undoubted interests of their constituents."<sup>6</sup>

The view of Mr. Madison that retrospective legislation was contrary to sound legislative principles seems to have been the basis of the separate opinion of Justice Johnson in the very early and important case of *Fletcher v. Peck*.<sup>7</sup> He says:

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<sup>5</sup> The *Federalist*, No. 7.

<sup>6</sup> *Federalist*, No. 44.

<sup>7</sup> 6 Cranch. 87 (1810).

"I do not hesitate to declare that a state does not possess the power of revoking its own grants. But I do it on a general principle, on the reason and nature of things: a principle which will impose laws even on the Diety. . . . I have thrown out these ideas that I may have it distinctly understood that my opinion on this point is not founded on the provision in the Constitution of the United States, relative to the laws impairing the obligation of contracts."

It is of some interest as to the early conception of the clause, however, to note that he regards the provision as being too equivocal to form the basis of restricting the states' power to interfere in private contracts. He adds:

"To give it the general effect of a restriction of the state powers in favor of private rights, is certainly going very far beyond the obvious and necessary import of the words, and would operate to restrict the states in the exercise of that right which every community must exercise."

It is apparent that in this regard Justice Johnson lacked the prescience of a Madison and the fatal logic of a Marshall.

Mr. Bancroft in his *History of the Constitution of the United States* explains the purpose back of the contract clause in the following statement:

"Any man loaning money or making a contract in his own State or in another, was liable at any time to loss by some fitful act of separate legislation. The necessity of providing effectually for the security of private rights and the steady dispensation of justice, more, perhaps, than anything else, brought about the new Constitution."<sup>8</sup>

This would seem to be more nearly in harmony with the interpretation of Mr. Madison but, on the other hand, a reference to Tucker on the Constitution is more in accord with the Hamiltonian interpretation. He says:

"The power of this prohibition was to maintain the integrity of contracts between citizens of different States and portions of the Union. If any State could, at its will, impair the obligation of a contract between its own citizens and citizens of other States, it would be a fatal impediment to interstate commerce and Federal intercourse."<sup>9</sup>

These various authorities merely emphasize the extent of the confusion that existed, and even continues to exist, as to the real purpose back of the contract clause and the ends it was pro-

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<sup>8</sup> Hist. of Const. of U. S., Vol. I, book 2, c. 6.

<sup>9</sup> Tucker, Const. of U. S. 828.

posed to accomplish. Perhaps its full significance was not realized by the Convention. As was said by Mr. Cooley:

"It is remarkable that this very important clause was passed over almost without comment during the discussions preceding the adoption of that instrument, though since its adoption no clause which the Constitution contains has been more prolific of litigation, or given rise to more animated and at times angry controversy."<sup>10</sup>

Obscure its origin may have been; uncertain the purpose that brought it into being; yet, the contract clause is inseparably connected with the early development of our constitutional history, and in the hands of John Marshall became a vital cog in the elaborate scheme of federal supremacy.

#### EARLY DEVELOPMENT

The first reference to the contract clause in the Federal Courts is in the case of *Champion and Dickason v. Casey*,<sup>11</sup> decided by Jay, Cushing and District Judge Marchant in 1792, sitting in the Circuit Court for the District of Rhode Island. The case involved the exemption of the person from arrest and the estate from attachment for a period of three years under an insolvent law designed as a protection to debtors. This law (as applied to pre-existing debts) was held unconstitutional as impairing the obligation of contracts.

Another very early reference to the clause in the Federal Courts was made by Marshall, sitting in the Circuit Court for the District of North Carolina in the case of *Ogden v. Nash*,<sup>12</sup> in 1802. A question arose as to whether a statute of limitations of 1715 had been repealed by an act of 1789. To settle the point the legislature of North Carolina in 1799 passed a law which provided that the act of 1715 has continued and shall continue in force. After holding the act of 1799 to be an invasion of the judiciary by attempting to pass legislatively upon the legal effect of the repealing act of 1789, Marshall added these words:

"It seems also to be void for another reason; the federal Constitution prohibits the States to pass any law impairing the obligation of contracts. Now will it not impair the obligation, if a contract, which, at the time of passing the act of 1789, might be recovered on by the creditor, shall by the operation of the act of 1799, be entirely deprived of his remedy?"

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<sup>10</sup> Cooley, Const. Limitations, 8th Ed. 554.

<sup>11</sup> Warren, Sup. Ct. in U. S. Hist., Vol. 1, 67.

<sup>12</sup> 2 Haywood (N. C.), 227 (1802).

The effect of the North Carolina legislation was passed upon by the Supreme Court of the United States in the case of *Ogden v. Blackledge*<sup>13</sup> which was certified to the Court from the District Court of North Carolina, due to the difference of opinion held by Marshall and Justice Potter. The opinion of the Supreme Court was delivered by Cushing but the point in the case was decided without reference to the contract clause.

The first decision of the Supreme Court holding a state law void as being an impairment of the obligation of contract was that of *Fletcher v. Peck*,<sup>14</sup> decided in 1810. The question in the case was whether a legislative grant was a contract that fell within the protection of the contract clause. The history of the case seethes with fraud and corruption among the members of the Georgia legislature who had granted away more than thirty-five million acres of land for a little more than a cent an acre. After demonstrating that the clause protects both executed and executory contracts, Marshall continues:

"If under a fair construction of the Constitution, grants are comprehended under the term contracts, is a grant from the State excluded from the operation of the provision? Is the clause to be considered as inhibiting the state from impairing the obligation of contracts between two individuals, but as excluding from that inhibition contracts made with itself? The words themselves contain no such distinction."

Therefore the repealing grant of the Georgia Legislature was held void as impairing the obligation of contract under the Constitution of the United States. Reference to the separate opinion of Justice Johnson in this case has already been made.

Two years later the Supreme Court applied the contract clause as a limitation upon state legislation in the case of *State of New Jersey v. Wilson*.<sup>15</sup> There was involved the question as to whether legislative tax exemption constituted a contract and the decision was in the affirmative. Marshall cited the case of *Fletcher v. Peck* (supra) as decisive of the question and without hearing of argument delivered the opinion of the Court:

"The act (repealing the exemption), in the opinion of this Court, is repugnant to the Constitution of the United States, in as much as it impairs the obligation of contract, and is, on that account, void."

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<sup>13</sup> Cranch, 272 (1804).

<sup>14</sup> 6 Cranch, 87 (1810).

<sup>15</sup> 7 Cranch, 164 (1812).

Just as in these two cases the sanctity of contracts was upheld where a state and individuals were parties, so in the case of *Sturges v. Crowninshield*<sup>16</sup> the protection was afforded to a contract as between two individuals. In this case the Supreme Court held that a New York bankrupt law was without effect to discharge a debtor from liability for a debt contracted prior to the passage of the law, since it would serve to impair the obligation of contracts. It was accordingly decided that the discharge was no defense to an action on the debt. In the course of his opinion, Marshall said:

"The fair, and, we think, the necessary construction of the sentence requires, that we should give these words their full and obvious meaning. . . . The Convention appears to have intended to establish a general principle, that contracts should be inviolable."

Just before his opinion in the above case, however, Marshall had delivered his opinion in the famous case of *Dartmouth College v. Woodward*,<sup>17</sup> holding that a corporate charter was a contract within the constitutional provision relating to contracts, and that a state legislature was without the power to impair the obligation of the same.

The history of the case as stated by Mr. Bevrige<sup>18</sup> shows that Mr. Webster and even members of the Supreme Court were doubtful if the protection to the charter could be based upon the contract clause. Mr Webster, in his argument of the case, emphasized general principles of abstract justice. He quoted Madison's statement from the Federalist (*supra*) declaring that such laws interfering with contracts "are contrary to the first principles of the social compact, and to every principle of sound legislation." A division of opinion resulted which led the Court to continue the cause. Before rehearing, all of the Justices except Duval and Todd had reached an agreement and Marshall had prepared his opinion. To prevent the reopening of the case the Chief-Justice, upon the convening of the Court at the next term, pitched into the reading of the opinion while Mr. Pinckney, who had been retained by the "University" during the adjournment, was in the act of addressing the Court to ask for

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<sup>16</sup> 4 Wheaton, 122 (1819).

<sup>17</sup> 4 Wheaton, 518 (1819).

<sup>18</sup> Life of John Marshall, Vol. IV, 220-281.



a reargument.<sup>19</sup> Despite the earlier fears of Mr. Webster and even Justice Story as to the application of the contract clause, Marshall, with characteristic boldness, declared the charter to be a contract and then proceeded to make one of the most sweeping and able arguments for contract inviolability that was ever pronounced. He observed:

"This is plainly a contract to which the donors, the trustees, and the crown, (to whose rights and obligations New Hampshire succeeds), were the original parties. It is a contract made on a valuable consideration. It is a contract for the security and disposition of property. It is a contract, on the faith of which, real and personal estate has been conveyed to the corporation. It is then a contract within the letter of the Constitution, and within its spirit also, unless the fact, that the property is invested by the donors in trustees for the promotion of religion and education, for the benefit of persons who are perpetually changing, though the objects remain the same, shall create a particular exception, taking this case out of the prohibition contained in the Constitution. . . . On what safe and intelligible ground can this exception stand? There is no expression in the Constitution, no sentiment delivered by its contemporaneous expounders, which would justify us in making it."

Thus, in the brief space of a decade, Marshall, with his consummate skill as an analyst and logician and his passionate devotion to stability, had taken the contract clause from its obscure and confused origin and made it one of the most vital of all the constitutional provisions. So well was the task performed that succeeding generations of the judiciary have largely been engaged in the process of restriction and limitation of the clause in the interest of legitimate legislative discretion and control.

#### SUBSEQUENT LIMITATION

The first significant limitation upon the provision came from the decision in *Charles River Bridge v. Warren Bridge*,<sup>20</sup> involving the constitutionality of an act of the Massachusetts Legislature of 1828, granting a charter to the defendant corporation for the erection of a free bridge in competition with a toll bridge operating under an unexpired charter. The case was first argued before the Supreme Court in 1831 but was not decided. In 1832 it was ordered continued. Mr. Warren makes this reference to the case:

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<sup>19</sup> Life of John Marshall, Vol. IV, 261.

<sup>20</sup> 11 Peters 420 (1837).

"It seems as the Court stood in 1832, Story, Marshall, and Thompson were in favor of reversing the decree of the Massachusetts Court (upholding the free bridge), McLean was doubtful of jurisdiction, Baldwin dissented, and Johnson and Duval had been absent. When the case was decided in 1837, seven judges took the contrary view, and Story and Thompson dissented."<sup>21</sup>

There is evidently some error in this reference to the case by Mr. Warren. Instead of there being seven judges taking a contrary view, their were only four. Story and Thompson held to their former view and so dissented. McLean retained his opinion that the Court was without jurisdiction but on the merits of the case agreed with Story and Thompson in favoring the toll bridge. In fact, at the time of this decision in 1837, there were only seven judges in all on the Supreme Court. The two extra judges were not appointed until two months after the decision and took their seats in the 1838 term. It is certain, however, that the deaths of Marshall and Johnson, coupled with the resignation of Duvall, had so changed the complexion of the Court as to make the decision directly contrary to what would have been decided by the Court as constituted in 1832. The newly appointed Chief Justice, Taney, delivered the opinion of the Court:

"The whole community are interested in this inquiry, and they have a right that the power of preventing their comfort and convenience, and of advancing the public prosperity, by providing safe, convenient, and cheap ways for the transportation of produce, and the purposes of travel, shall not be construed to have been surrendered or diminished by the state; unless it shall appear in plain words, that it was intended to be done."

Thus was established the foundation for one of the most far-reaching limitations upon the decision in the Dartmouth College case that the Court has ever pronounced. Under the doctrine of strict construction all doubts were henceforth to be resolved in favor of the state and against the grantee. Mr. Webster was greatly chagrined at the decision in the face of his masterly argument before the Court. He wrote:

"The decision of the Court will have completely overturned, in my judgment, a great provision of the Constitution."<sup>22</sup>

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<sup>21</sup> Warren, Hist. Sup. Ct., Vol. II, 233, footnote.

<sup>22</sup> Warren, Sup. Ct. in U. S. Hist., Vol. II, 299.

That there was some basis for the fears of Mr. Webster is shown by the case of *Covington v. Kentucky*,<sup>23</sup> where the Supreme Court applied the doctrine of strict construction to a legislative grant of tax exemption. The grant to the Water Co. provided:

"Its property shall be and remain forever exempt from state, county and city tax."

The Court held, however, that the grant contained no plainly expressed intent never to amend or repeal it. Evidently the Court was not much impressed by the use of the word "forever," since it decided that the implication from the grant was "forever, unless the legislature should change its mind."

Another case of some interest in the application of the doctrine of strict construction as applied to the contract clause is that of *Newton v. Commissioners*<sup>24</sup> decided by the Supreme Court. An act of the legislature of Ohio in 1846 provided that the county seat in Mahoning County should be "permanently established" in Canfield. The terms were met and the county seat established in Canfield. By a subsequent act of the legislature it was removed. James A. Garfield argued for the city that the subsequent legislation violated the obligation of a contract. He quoted from a previous decision of the Court to show that:

"The rule that legislative grants and contracts are to be construed most favorably to the State does not tolerate the defeating of the grant or contract by any hypercritical construction."

The Supreme Court decided, however, that the "county seat was permanently established at Canfield when it was placed there with the intention that it should remain there. It fulfilled at the outset the entire obligation it had assumed. Keeping it there is another and distinct thing."

Of course, the real justification for this decision rests upon the correct and accepted theory that the establishment of county seat is a governmental function, the free exercise of which cannot be limited by prior grant or contract. This is still another limitation upon the contract clause. The difficulty lies not in the statement of the rule, but in deciding its proper application.

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<sup>23</sup> 173 U. S. 231 (1899).

<sup>24</sup> 100 U. S. 548 (1879).

Still another limitation upon the provision is the power of eminent domain. The case of *West River Bridge Co. v. Dix*<sup>25</sup> will best serve to illustrate this principle. In holding that a bridge, held by an incorporated company, under an unexpired charter from the state, may be condemned and taken as a part of a public road, under the laws of the state. The Supreme Court, speaking through Justice Daniel, said:

"Into all contracts, whether made between States and individuals or between individuals only, there enter conditions which arise not out of the literal terms of the contract itself; they are superinduced by the pre-existing and higher authority of the laws of nature, of nations, or of the community to which the parties belong; they are always presumed, and must be presumed, to be known and recognized by all, are binding upon all, and need never, therefore, be carried into express stipulation, for this could add nothing to their force. Every contract is made in subordination to them, and must yield to their control, as conditions inherent and paramount, wherever a necessity for their execution shall occur. Such a condition is the right of eminent domain."

It is rather remarkable that while the right of eminent domain is so readily accepted by the profession today as a matter of course, that Mr. Webster, in his argument of this case in 1848, could contend with all earnestness:

"This power, the eminent domain, which only within a few years was first recognized and naturalized in this country, is unknown to our Constitution or that of the State (Vermont). It has been adopted from writers on other and arbitrary governments. If the Legislature or their agents are to be the sole judges of what is to be taken, and to what public use it is to be appointed, the most levelling ultraisms of Anti-rentism or Agrarianism or Abolitionism may be successfully advanced."

The contract clause might stagger along with some manifestation of vitality, however, were it subject only to the limitations of strict construction and eminent domain. There is a third limitation, however, that has all but stripped it of its vast importance. This limitation is that of the police power. The first clear-cut case coming before the Supreme Court where the supremacy of the police power was asserted is that of *Stone v. Mississippi*.<sup>26</sup> The point involved was the right of Mississippi to prohibit lotteries by constitutional provision, in the face of an

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<sup>25</sup> 6 Howard 507 (1848).

<sup>26</sup> 101 U. S. 814 (1880).

unexpired legislative charter grant to a lottery corporation, made upon the receipt of a stipulated consideration which had been paid. Waite delivered the opinion of the Court:

"No legislature can bargain away the public health or the public morals. The people themselves cannot do it, much less their servants."

The police power of the state was flatly declared to be paramount to the contract clause of the federal Constitution. In line with this and similar decisions the states are now permitted to engage in legislative regulations and prohibitions affecting contract rights that would have unquestionably been declared void in the early period of the Supreme Court. The vast importance of the limitation lies in the ever expansive definition that is attached to the term. Where, historically, the police power has been regarded as embracing "health, safety and morals," it is now given a much broader interpretation and is made to include economic consideration. Practically every case of justifiable legislation could be placed within the broad scope of existing definitions.

The case of *Illinois Central Railroad Co. v. Illinois*<sup>27</sup> involved a grant, from the state of Illinois to the railroad, of the bed of Lake Michigan along the Chicago coast line. The Supreme Court upheld the right of the State to repeal the grant despite the fact that it was made upon a consideration paid by the grantee. Evidently no question of health, safety or morals determined the case. Manifestly, however, the grant was economically unwise. Justice Field, in his opinion, said:

"We cannot it is true cite any authority where a grant of this kind has been held invalid, for we believe that no instance exists where the harbor of a great city and its commerce have been allowed to pass into the control of any private corporation. But the decisions are numerous which declare that such property is held by the State, by virtue of its sovereignty, in trust for the public."

The repealing act was, therefore, upheld. It is apparent that the invalidity of the grant was based upon the extent of the property involved. Still, it is hard to see why this grant presented any more evidence of invalidity than the grant in *Fletcher v. Peck* (supra) involving thirty-five million acres of fertile lands. Economic factors now seem to outweigh the strictures of pure logic.

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<sup>27</sup>146 U. S. 387 (1892).

Still another case will serve to show the extent to which the Supreme Court has gone in its widened conception of the police power as being something more than a protection of the health, safety, and morals of the public. In *Atlantic Coast Line R. R. Co. v. Goldsboro*<sup>28</sup> the Court says:

"It is settled that neither the contract clause nor the due process clause has the effect of overriding the power of the State to establish all regulations that are reasonably necessary to secure the health, safety, good order, comfort, or general welfare of the community; that this power can neither be abdicated nor bargained away, and is inalienable even by express grant; and that all contract and property rights are held subject to its fair exercise."

It was this tendency of the Supreme Court to indulge in sweeping generalizations as to the extent of the police power that led Mr. Freund, an eminent authority in this field of the law, to remark:

"If there is anything left to the contract clause of the Constitution of the United States, it would take a magnifying glass to find it."

The decision of the Supreme Court in the case involving the New York Housing law is a recent example of the modern theory. In this case<sup>29</sup> a law of New York was upheld which directly interfered with existing contracts by allowing a tenant to retain possession of the premises under an expired lease which carries with it a covenant to surrender. The Court found its justification in the post-war necessity for housing regulation in the interest of the public welfare.

It will be interesting to note whether the Court will continue to subordinate the contract clause to an elastic and ever expanding police power, or whether there will follow a period of reaction that will serve to vitalize and emphasize the provision. As matters now stand the protection of the clause goes very little beyond the protection of the due process clause. Since Congress is subject to this limitation also, perhaps we have unconsciously drifted back to the apparent intent of the Constitutional Convention to place both Congress and the states under similar restrictions, so far as interfering with contracts is concerned.

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<sup>28</sup> 232 U. S. 548 (1914).

<sup>29</sup> 256 U. S. 170 (1921).